Vietnam's Legal Framework for Foreign Investment

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I. Introduction

Since 1991, Vietnam attracted a high volume of foreign investments as a result of policy reform toward market economy introduced in the late 1980s. However, Vietnam's foreign investments are mired with problems both for the host country and for investors coming to Vietnam. To the dismay of the government, foreign investments projects in Vietnam are characterized by a) a high concentration in a few subsectors such as oil and gas and hotels, i.e. in low-risk projects instead of diversified investment in manufacturing; b) more significantly, a low rate of implementation of about thirty percent of investments approved. Low rate of implementation thus creates a high level of approved investment (investments committed), which is deceptive. To the many foreign investors who had to deal with many problems of Vietnam's bureaucracy in trying to get their projects approved and implemented a decade of trying to make profit in the emerging market of Vietnam is a decade of time lost and of disappointment.

This article suggests that the slow implementation of projects was due in part to problems within the country's current legal framework, which also caused a sharp decline in the level of foreign investments commitments for the last two years. Foreign investors had hoped for significant reform of the legal framework and that related policies would be undertaken, but the government has been slow to respond to their concerns. Vietnam's unstable legal framework and regulatory impediments seem to have prevented serious investors, particularly those coming from the West, from implementing high-risk, long-gestation projects. The legal fatigue has made a few foreign investors give up on Vietnam.

Vietnam's legal system for foreign investments contains a special regime featuring tax and other incentives for foreign investments. It is a legal enclave. Apart from several specific problems within this enclave, the larger issue is whether the concept of legal enclave is a good one for Vietnam. This article argues that the concept of legal enclave can be useful

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in the short-run to attract foreign investments, but in the long run the enclave should be phased out, as a sound investment climate made of a stable legal framework and a general deregulation policy is preferable to enclave strategy.

II. Scope

This study will first briefly review Vietnam's Reform Program (Doi-Moi or Renovation) designed to transform its command economy into a market economy[1] and assess foreign investments performance as a result of this changed policy. The following section will analyze Vietnam's 1989 Foreign Investments Law and recent amendments, including the latest amendments introduced in November 1996; the analysis will focus on the legal enclave nature of Vietnam's foreign investments regime. Next, the article will assess regulatory issues, particularly Vietnam's process of foreign investments approval, which has been the most serious and continuing problem for foreign investors in Vietnam. Then it turns to some substantive law issues pertinent to foreign investments, such as corporate governance in joint venture projects and land use rights. An evaluation of important issues of Vietnam's law enforcement including the court system, adjudication method, particularly the resolution of commercial disputes which form the country 's legal infrastructure, is included along with a review of the country's emerging legal profession and reformed legal education system.

To help Vietnam policy-makers improve their nascent legal framework, the article adopts the broad approach to deal with generic issues of Vietnam's legal framework in transition, that is, issues related to Vietnam's efforts to establish the Rule of Law in contrast to its Rule by Decree during the war. The article will, however, attempt to address these issues in a practical way, in some detail, with an eye to making it useful to practicing lawyers, particularly those who are taking on Vietnam cases or projects for the first time.

III. Vietnam's Reform Program For Transition and Foreign Direct Investment in Vietnam: An Overview

Vietnam started its transition to a market economy in 1989 with a fundamental reform program known as the Renovation (Doi Moi).[2] With the objective of transforming its centrally planned economy into a market system, the program included primarily: (a) a macroeconomic stabilization program including a liberalized foreign exchange; (b) a broad-based price reform including the elimination of subsidy to state-own enterprises (SOE); and (c) a new legal framework that permitted for the first time foreign investments and reactivation of domestic private businesses.

The Foreign Investments Law promulgated in 1987 amended in 1990, 1992 and most recently in November 1996, was the key element of the reform program. Private domestic investment was also allowed beyond the micro-enterprise scale, but it was not perceived by the government as important as direct foreign investments (FDI); the latter was expected

1. Vietnam's reform program has been analyzed in detail by numerous academic institutions and international organizations. For a short analysis of this program, see PHAM VAN THUYET, GEO. MASON U. INDOCHINA INST., VIETNAMESE ECONOMY: PERFORMANCE AND PROSPECTS, AN OVERVIEW (1992).

2. *See id.* at opt. cite, n. 1 (citing VIET-NAM: TRANSITION TO THE MARKET, AN ECONOMIC REPORT, WORLD BANK REPORT No. 11902-VN, (1993)).

to jump-start an economy that had been in distress as a result of the abrupt termination of Soviet Aid following the collapse of the former Soviet Union. The market-oriented reform brought high growth of output and until 1995, a steadily increasing inflow of foreign direct investment (Table 1).

The flow of foreign investments started to slow down in 1996 until the final week of December when the government, in an effort to maintain the increasing trend of FDI inflow, allegedly approved two large urban development projects worth $3,263 million amidst loud complaints about problems with investing in Vietnam. These last-minute FDI approvals represent thirty-eight percent of the year's total. But FDI declined by about fifty percent in 1997 and continued to fall further in 1998. This decline in foreign investments, coupled with reduced exports and other negative impacts of the current financial crisis in Asia have contributed to a reduction of overall economic growth, from a decade's high rate of nine percent per year to the current four to five percent.[3]

FDI in Vietnam has been narrowly based, mainly in hotel projects and in capital-intensive industries, such as oil projects. For example, out of $1,700 million FDI committed during the first nine months of 1998, $700 million, or forty-one percent, came from one project, a resort development scheme. Over the years, FDI flow to manufacturing has been limited; a situation similar to when China began to implement its FDI development program in the early 1980s.[4] As a result, FDI in Vietnam has contributed little to transfer of technology

Table 1
Vietnam: Foreign Investments Approved 1988–1998

	Number of projects	**Investment Amount (US$ million)**
1988	37	366
1989	70	539
1990	111	596
1991	155	1,388
1992	193	2,271
1993	272	2,987
1994	362	4,071
1995	404	6,616
1996	326	8,538 (38% approved in the final week of December, from 5,260 million)
1997	270	4,500
1998 (as of October)	181	1647

Source: Ministry of Planning and Investment (MPI), formerly State Committee of Cooperation and Investment (SCCI), published in *Vietnam Investment Review*, September 15, 1997 (for data throughout December 1997) and October 15,1998 issue for 1998 data (as of October).

3. For an analysis of Vietnam's current economic situation, see Pham Van Thuyet, Vietnam: A Tiger or Wild Cat?, (Nov. 1997) (unpublished paper on file with Columbia University); Pham Van Thuyet, Deepening Reform for Growth, An Economic Report (Oct. 1997).

and employment generation, areas in which more manufacturing industries would have greater effects.

A. Pattern of Foreign Investments

Most of the largest projects approved are in oil and gas exploration, located in the southern coastal town of Vung-Tau. Tourism industry activities are visible in large cities where several big, internationally known hotels, among the 250 proposed hotel projects, have been built. Also popular are consumer electronics assembly for local market and export-oriented projects using low-cost labor in light industries, such as garments and footwear. While assembly plants for consumer electronics have been set up mainly by the Japanese and Koreans, garment and footwear industries have been developed by investors from Taiwan, Hong Kong, Singapore, and Korea who brought in equipment, fabrics, and other materials to produce final goods for export.

Over the years, Singapore, Taiwan, Korea, and Hong Kong alternatively took the lead in FDI in Vietnam. In October 1998, with a cumulative total investment of $6,447 million approved, Singapore was the leading country in FDI followed by Taiwan, which in 1996 was the leading country. Singapore and Taiwan, along with Hong Kong, Japan, and South Korea constitute the five leading countries in foreign investments in Vietnam (Table 2). U.S. investors started to arrive following the lifting of the U.S. trade embargo against Vietnam. The arrival of the first U.S. ambassador to Vietnam in May 1997 has raised some

Table 2
Vietnam: Foreign Investments by Countries, cumulative as of October 1998

Ranking	**Country**	**Number of Projects**	**Investment Amount (US$ million)**
1	Singapore	181	6.447
2	Taiwan	309	4,268
3	Hongkong	184	3,734
4	Japan	213	3,500
5	South Korea	191	3,154
6	France	89	1,465
7	Malaysia	59	1,370
8	US	70	1,230
9	Thailand	78	1,109
10	British Virgin Island	55	1,089

Source: Ministry of Planning and Investment (MPI) published in *Vietnam Investment Review*, October 1998.

4. For an analysis of China's FDI program, see Zafar Shah Khan, Patterns of Foreign Investments in China, World Bank Discussion Papers Series, No. 130 (1991).

expectations of more U.S. investment to follow, but U.S. investors are still cautious in view of the slow implementation of FDI in general and feedback about problems encountered by early investors.

The United States ranked eighth by October 1998, sixth in 1997, among foreign countries investing in Vietnam. Countries in the former European Socialist Block have no significant investments in Vietnam except the former Soviet Union, which has thirty-five projects approved of which thirty belong to Russia, totaling $188 million. Japan, while a major trading partner with Vietnam, had relatively small share in FDI for many years (about $100 million prior to 1993) in part due to Japan's cautious policy in consideration of the U.S. trade embargo. Japan has increased its share considerably, ranking fourth by October 1998.

About two-thirds of FDI proposed are for projects located in the south, despite Government's encouragement and promotion of investment in the northern part of the country. Foreign investors prefer to have their projects located in the south where, among other things, the infrastructure is more developed than in the north and business practice as known in the West is also better understood. Management skills appropriate to market economy, although in short supply in both the north and south are nevertheless more available in the latter.

Like China, the majority of Vietnam's foreign investment projects are joint ventures, with State Owned Enterprises (SOE) or state agencies who almost always contribute their capital in the form of land-use rights. A 1992 revision of DFI Law allowed private companies to enter joint ventures with foreign investors. The DFI Law also allows for 100 percent foreign-owned projects, but relatively few of the approved projects are of this type.

B. High Volume of Commitments and Slow Implementation

Despite a high volume of FDI commitments or approvals, implementation of projects has been slow, averaging about thirty percent over the years in value terms. Data on implementation are hard to come by as the former State Committee for Cooperation and Investment (SCCI), now integrated into the Ministry of Planning and Investment, the main agency in charge of FDI, is still working to improve a system for monitoring project implementation. Yet, aggregate data indicate an annual rate of current year's implementation to previous year's sanctioning of around thirty percent, assuming projects would start to be implemented between six months and one year after being sanctioned. (The DFI Law required that DFI projects be implemented six months following approval). Disaggregated data compiled on a project basis[5] also confirmed this low rate of implementation (Table 3).

Project implementation in the oil sector, as in the hotel construction sector, seems to be the most active as over $400 million have been spent among the twenty-four licenses issued for exploration in oil or gas. In addition to oil exploration, bidding for oil refineries has been very active from seventeen bidding companies. In addition to Japan, France and Canada (liquid gas), other countries interested in oil exploration in Vietnam are the newly industrialized countries (NIC) of Korea, Taiwan and Malaysia.

5. *See* Kwang W. Jun, Duc Minh Pham, Victoria Kwakwa, Kyle Peters, Jr., & Thang-Long Ton, Foreign Capital Flow In Vietnam, World Bank (1997).

Table 3
Vietnam: Implementation of Foreign Investments Projects, 1991–1998

Year (amount in US $ million)	1991	1992	1993	1994	1995	1996	1997	1998 (est.)
Commitment (Approved)	2,889	2,271	2,987	4,071	6,616	8,500	4,500	2.300
Implementation	620	463	1,002	1,500	2,000	1,800	2,600	1,500
Implementation as percent of approvals (%)	21.5	20.4	33.5	36.8	30.2	21.0	58.0	65

Source: Ministry of Planning and Investment (MPI). Data 1996–1998 from the World Bank, which used the same source of MPI.

C. Vietnam Pullout: This Time It Is the Early-Bird Investors

Vietnam Pullout, as heralded in the June 24, 1998, *Wall Street Journal*, was the title of one of several recent newspaper accounts of declining foreign investments in Vietnam. After several years of high growth generated in part by a high volume of foreign investments, Vietnam's growth has slowed down. Foreign investments have declined to about half of the average over the first five years following the 1989 reform. Several investors, including some big-name companies such as Chrysler, Hyundai, and the French Oil Company Total, are pulling out of Vietnam. They represent the first wave of daring investors who jumped in when Vietnam first opened its market to foreign investors. They have waited for real reform to bring about a better investment climate to begin implementing their approved projects. The reform, in the opinion of many observers has produce too little, too late. Chief among the required changes is reform of the legal framework to provide some security in transactions for investors, including reform of property law, contract law, company governance, and the enforcement of existing laws. The need for such reform of the legal and regulatory framework has been voiced at various conferences and evidenced by studies done over the last ten years. It is in this context that this article assesses Vietnam's legal framework for foreign investments, focusing on its problems and areas for improvement. Improvements in the legal system and other policy areas are needed if Vietnam intends to lure back foreign investors, to increase investment and to return to the high rate of growth it has experienced for a decade. Once the Asian crisis subsides, the prospect of Vietnam reemerging as a high-growth country is not unrealistic, given the country's comparative advantages of a literate population, an abundance of labor, and a well-balanced endowment of natural resources.

IV. Vietnam's Enclave-based Strategy on Foreign Investment: The Emerging Legal Framework for FDI

This section reviews some of the more important aspects of Vietnam's legal framework for FDI as set out in the Foreign Investments Law. [6] The latest amendments passed by Parliament, which took effect on March 1, 1997, were considered by the government to be the new statute on FDI—formally called Law on Foreign investments in Vietnam because

6. The original statute of 1987 was amended in 1990, 1992 and most recently on November 8, 1996.

they were perceived by the government as extensive enough to replace the old law as a whole. With a few changes, the new law retains most of the provisions of the old one. The subsequent sections of this article will also discuss relevant parts of other laws and regulations, particularly regarding land use rights, trade laws, labor laws, and banking regulations, since the Foreign investments Law does not cover all aspects of the legal framework for FDI.

A. The Legal Enclave: A System of Special Tax Privileges and Other Incentives for Foreign Investments

Vietnam's current legal framework for FDI constitutes a legal enclave in that a special regime featuring both privileges and restrictions governs all FDI. The physical enclave in the form of fenced Export Processing Zones (EPZ) supplements the legal enclave strategy. The legal enclave for FDI in Vietnam was established by a set of laws and administrative rules different from the company laws governing the formation and functioning of domestic companies, and a package of special incentives benefiting FDI that is not available for domestic investors.

In general, Vietnam's system of special incentives for FDI in substance is comparable to that of countries of the Association of South East Asia (ASEAN) and South Asia countries (Table 4), and also comparable to China's incentives package. Regarding tax holidays, Vietnam's two-year treatment is more favorable than that of Eastern European countries, which also have a two-year tax holiday but tax rates are commonly set at forty percent[7], higher than Vietnam's twenty-one to twenty-five percent rates.

B. Tax Incentives

The fiscal incentives package consisting of (a) a tax holiday of up to two years plus another two years at fifty percent of the tax level; (b) preferential corporate income tax rates between ten and fifteen percent (less than the normal twenty-one to twenty-five percent rates) for FDI in the priority categories; and (c) machinery, equipment and raw materials, if used for export industries, are exempted from import duties.

FDI that meet two of the following criteria are treated as investments in the priority categories for the purpose of lower tax treatment:

1. Legal capital of the enterprise is not less than $10 million (U.S.);
2. Technology transfer to the enterprise meets at least two of the requirements[8]; namely: (a) it is capable of bringing about a considerable improvement in the form and quality of products, and an increase in output; (b) the method of production is safe; (c) it will make rational use of energy, natural resources and manpower; and (d) it will not adversely affect the environment.
3. The project should export at least eighty percent of its products or earn at least eighty percent of its revenue in foreign currencies;
4. The rate of profits of the project is low compared with the average rate obtained in other projects in the same area;

7. Cheryl W. Gray & William Jaroz, Foreign Investments Law in Central and Eastern Europe, World Bank Working Paper No. 1111, 18 (1993).

8. Vietnam, Ordinance on Transfer of Foreign Tech., art. 4 (Dec. 5, 1988).

Table 4
Vietnam: Direct Foreign Investments, Comparative Incentives with Asean and South Asia Countries

ASEAN countries	Tax Incentives	Import Tariff	EPZ and/other Free Trade Instruments	Other Incentives
Indonesia	None	Duty drawback	Bonded zones	Joint ventures required of DFIs
Malaysia	Five-year tax holiday	Exemption for machinery and raw materials for approved projects.	Several EPZs	Loans from government-sponsored banks available R & D expenditures tax deductible
Philippines	Five to eight years tax holiday	–Exemption for machinery –Post-operative tariff protection available	Several EPZs	Tax incentives for projects in underdeveloped areas-R & D expenditures tax deductible
Singapore	Five to ten years tax holiday	–Exemption for nearly all imports including for FDI.	Several Free Trade Zones	–Loans at concessionaire rates for targeted industries –R & D expenditures tax deductible
Thailand	Three to five years tax holiday	Exemption for machinery and selected raw materials	Two EPZs	–Tax credits for projects outside Bangkok –Infrastructure support for large projects
Vietnam	Two year tax holiday plus two year of tax exemption at 50%	Exemption for machinery and raw materials for approved projects	–Two EPZ. Other EPZ planned	–Reduced corporate tax rate for FDI on "priority industries" list. Incentives for industries in backward regions. –100% owned FDI allowed

Table 4
Continued

ASEAN countries	Tax Incentives	Import Tariff	EPZ and/other Free Trade Instruments	Other Incentives
South-Asia Countries:				
India	Five year tax holiday	Tariff protection for local industries; easy access to imports for some industries	–Three free trade zones	–Subsidies for industries in backward regions and other incentives; R&D expenses tax deductible.
Pakistan	Tax-exempt for income of some industries, export profit; five year tax holiday for EPZ activities	Quota and high tariff competing imports; duty-free for machinery for some projects	–EPZ in Karachi	–Income tax exemption and other incentives for industries in backward regions; R&D expenses fully tax deductible
Sri Lanka	Five year tax holiday for certain industries	Import duty rebate for imports used for export industries	–Two EPZ with 10 year tax holiday and other incentives	–Export subsidies; capital spending in certain industries is tax deductible.

Sources: Vietnam: Foreign investments Law and Decrees (1991) 1992 and 1996 amendments. ASEAN countries and South Asia countries: **Doing Better Business in Asia** by *Business International*, a member of the Economist Group, Hong Kong

5. The project is located in a region where natural, economic and social conditions are unfavorable;
6. The investment is made within the first five years of implementation of the Law on Foreign investments.

This racing commitment method has probably been a contributing factor to the great inflow of FDI to Vietnam in the early 1990s, following the introduction of the FDI Law.

To compare with China's DFI strategy, which emphasizes technology and exports, Vietnam's DFI policy focuses on regional development in addition to export development and transfer of technology. Regional development has always been Vietnam's major concern as the northern half of the country is traditionally poorer than the south. The north has been pushed further backward as a result of long wars and mismanagement under centrally planned system for forty years. It should be noted, however, that experiences from other countries, particularly from South Asian countries where the concept of regional development by special incentives is very popular, show that promoting regional development through special incentives packages has not been successful. Vietnam has its own experience in the notorious case of the oil refinery project Dung-Quat, named after a district in the poor province of Quang-Ngai in Central Vietnam where infrastructure and other facilities are lacking. The area is 500 miles from the oil field and also prone to typhoon. The case involved Total Oil & Gaz of France, which had the project approved but later withdrew it over a disagreement with the government's imposed location preference for Dung-Quat, on the basis of regional development priority—the project has now been taken over by the Russian company RVO Zarubezhneft in a joint venture with VietPetro, a state-owned enterprise in oil and gas.

C. The New Law and the Old

Promulgated on November 8, 1996, followed by the application decree of January 1997 to take effect April 1, 1997, the new statute has sixty-eight articles, over twenty more articles than the old statute which has only thirty-eight articles. Except when indicated otherwise, the article numbers cited in this paper are provisions of the new statute. Most of the additional articles were introduced to elaborate some provisions of the previous statute. For example, article 58 formalized the role of local authorities in the process of approving FDI projects.

In terms of substantive law, the new version of the law has the following features:

a) In an effort to remove ambiguities, the new law uses the term direct foreign investments (article 2.1), as distinct from foreign investments in the language of the old law, which is commonly used in economics to mean investment in discreet projects, *i.e.*, projects in the real sector, as opposed to portfolio investment. This means that some of the provisions of this law such as tax incentives are not applicable to portfolio investment.
b) FDI enterprises can have a life of up to fifty years under article 17, instead of twenty years as under article 16 of the previous law. This provision simply codifies a 1992 amendment to the old statute.
c) Tax privileges, such as a two-year tax holiday, are extended to all FDI enterprises in article 39; article 27 of the old law provided this tax incentive to joint ventures only, i.e., excluding enterprises with 100 percent foreign-owned capital and contractual business cooperation.

d) The new law now allows existing joint ventures to invest in new joint ventures. Enterprises with 100 percent foreign-owned capital, however, must give first priority to Vietnamese nationals in transfer of the company's interests (article 34).

Foreign investors in Vietnam have been concerned about the bureaucratic process of FDI approval, corporate governance in joint ventures, and the unresolved issue of land-use rights. The new law addresses these areas of concern, but unfortunately the new provisions have not completely clarified the concerns. Some of the provisions, such as the one related to the power of local authorities, may raise more questions than answers.

D. Entry Laws and Exit Laws: The Forms of FDI

As part of the legal enclave, the new law retains three specific forms of business enterprises for FDI, joint venture enterprises, enterprises with 100 percent foreign-owned capital and Contractual Business Cooperation (CBC) (art. 4 of both the old and the new law). Except the provisions governing limited liability companies, Vietnam's company laws[9] generally are not applicable to FDI enterprises. As a result, FDI cannot be undertaken by an individual or sole proprietorship as provided in the Company Law. Further, the new law requires joint ventures as well as enterprises with 100 percent foreign-owned capital have to form under the French-type Limited Liability Company (SARL)[10] (arts. 6 and 15), which is a form of corporation usually used in companies with a restricted number of shareholders, such as family owned companies. Because shares in a SARL are not freely transferable, FDI enterprises are unable to raise capital by floating their shares in the local capital market once the Vietnam stock market is introduced. Foreign investors cannot own shares in a Vietnamese company since the company laws require shareholders to be Vietnamese citizens. This restriction, together with other regulatory requirements such as the submission of an economic feasibility study for discreet projects, in effect, bar FDI entry through buy-out or merger and acquisition.

Like in China, the majority, about eighty percent, of FDI in Vietnam are joint ventures formed mainly with SOEs. Less than five percent of FDI are 100 percent foreign owned and about fifteen percent are in contractual business cooperation enterprises. The latter were formed to carry out short-term, often one shot businesses, for example, one shipment of import or export cargo.

From a legal point of view, the contractual business cooperation enterprise, which in a way resembles a limited partnership, differs from joint ventures and 100 percent foreign owned FDIs in that contractual business cooperation does not create a judicial person or legal person. On the other hand, under the other two forms of FDI, a new judicial person is created under a limited liability enterprise, either as a limited liability company fashioned

9. Vietnam's Company Law and its application decrees are modeled upon the French Company Law to include (1) a "shareholding company"—similar to the French Société Anonyme (SA) and (2) a company with limited responsibility similar to the Société á Responsabilité Limité (SARL). Both types are companies of limited liability. For an analysis of Vietnam's Company Laws, see Pham Van Thuyet, *Legal Framework for Private Sector Development in Transitional Economies, The Case of Vietnam*, 27 Geo. J. L. & Pol'y Int'l Bus. 541 (1996).

10. For detailed discussion of French company law, *see, e.g.*, Georges Ripert & Rene Robot, *Traite de Droit Commercial*, Librairie de Droit et de Jurisprudence (Paris) (1991) or Alfred Jauffret, *Manuel de Droit Commercial*, Editions LGDJ (Paris) (1991). The provisions for SARL adopted in Vietnam Company Law were discussed in detail in Pham Van Thuyet's article cited in the preceding footnote.

after the French SARL, or a Corporation modeled upon the French Société Anonyme (SA). One implication is that contractual business cooperation enterprises are governed by contract law in addition to the Foreign Investments Law. In part because only a joint venture is entitled to tax exemption and tax holidays under the old law (arts. 27–28), FDI has been concentrated in joint venture enterprises.

To form a joint venture, foreign contribution must be at least thirty percent of total capital. Foreign partners should make their contribution in foreign exchange, while local investors' contribution can be in local currency but in most cases local contributions were in the form of land or land-use rights. Foreign investors can also make their contribution in the form of equipment and intellectual property, but in practice this type of contribution has been rare and predictably has caused long delays in approval as a result of difficult evaluation. Article 7 of the new law states that foreign investors can finance their participation in joint ventures in local currency if the local currency "were rooted in investment made in Vietnam." This is a reinvestment issue. The provision simply means that local currency earned or generated from a FDI project can be reinvested without first converting it into foreign exchanges; this in effect would lessen the burden on the government to provide foreign currency for the purpose of reinvestment.

E. Industries To Be Encouraged for Foreign Investments

Under Vietnam's policy, FDI should be a project that produces physical output, mostly new projects, reflecting the government's policy preference for productive undertaking (often understood as green field projects) as opposed to commercial comprador ventures, a label used in communist parlance.

Vietnam has sub-sector preferences for FDI, like China and many countries in South Asia where an outdated inward-looking strategy for development still survives. While China provides special incentives for FDI engaged in export-oriented industries and high-tech industries, article 3 of Vietnam's new law provides special treatment for a list of seven broad sub-sectors and regions where FDI is to be encouraged:[11]

1. Export-oriented industries;
2. Farming, animal husbandry, forestry development, and processing of agricultural, forestry and aquatic products;
3. High-technology industries and know-how industries; industries that protect environment or investment in Research and Development;
4. Labor intensive industries using raw materials and natural resources available in Vietnam;
5. Infrastructure; and important (undefined but presumably large scale or capital intensive) industries;
6. Investment in highland regions and remote areas;

11. According the old law (art.3), the list of priority industries includes five subsectors as follows: 1) large-scale industries, export-oriented and import substitution industries; 2) high-technology industries using skilled labor, investment for full employment and exploitation of potential resources available in Vietnam; 3) labor intensive industries using raw materials and natural resources available in Vietnam; 4) construction of infrastructure; and 5) foreign-exchange-earning service industries, such as tourism, ship repair, airport and sea port services, and other services.

7. Other underdeveloped regions defined as "having difficult socio-economic conditions."

Except for categories related to regional development, the new list of subsectors of priority industries is not too different from the old one. But two things are worth noting:

a) It has long been known to foreign lawyers or consultants counseling foreign investors in Vietnam that the government wants foreign investors to direct their investment to northern Vietnam, where economic development is lagging behind the south and poverty is much more pervasive.
b) The new list excludes "service paid in foreign exchange," such as tourism, ship repairing, and airport service, which in effect narrows the types of businesses in which foreign investors have a comparative advantage.

The use of priority lists, despite its apparent logic, is not a good idea even from Vietnam's perspective. As bureaucracy breeds itself, what in the beginning was defined to mean a non-binding list of encouraged industries has in many countries become a bureaucratic instrument of FDI screening, particularly for financial institutions' lending purposes. Experiences of countries, such as India, Pakistan, Sri Lanka, and Bangladesh, have shown that the use of lists, a by-product of the inward looking development strategies of the 1960s which were most popular in South Asia, has been ineffective and counter-productive in the long run. Vietnam should learn this lesson and abolish these lists.

Like the use of lists, the old-fashioned concept of using tax incentives to promote regional development has proven ineffective. Experiences by the same South Asia countries have shown that what investors need most is a reasonably good infrastructure, which is lacking in underdeveloped areas of the country, in addition to a stable legal framework. Tax incentives alone are not sufficient to lure investors to these areas. Vietnam experienced these problems when the French oil refinery project at Dung-Quat, mentioned earlier, was withdrawn.

F. Termination and Liquidation

In general, an FDI enterprise is established for a period of twenty years. The duration can be extended for up to fifty years for projects requiring a long gestation period and large investment. Most current projects are approved for twenty years.

While the procedure for normal termination is reasonably well established, it is not clear how Vietnam's bankruptcy law is applied to foreign investments enterprises. Joint ventures can be terminated by mutual agreement or upon expiration of the twenty-year period. In contrast to the dissolution procedure in the company laws, the dissolution of joint ventures, whether at expiration or prior to expiration of contract, is handled by a three-member liquidation committee, which is appointed by the board of directors to settle all pending obligations and liabilities of the enterprise. In the case of liquidation at expiration, a committee should be in place six months prior to the expiration date.

The FDI Law provides a guarantee against nationalization or expropriation and a guarantee for repatriation of capital and profits.

G. Repatriation of Capital and Transfer of Profit

1. *Repatriation of Capital*

Upon completion of the liquidation process, the remaining capital can be transferred abroad over three years in equal installments. This policy of transfer by installment reflects the government's concern over an orderly management of foreign exchange and foreign capital flows. Exceptions can be made to allow the transfer over a shorter period if the proposed remittance is small, currently one million dollars or less, or if the FDI enterprise has achieved eighty percent of the foreign exchange earnings budgeted. As FDI laws are new, and most projects have not been completed, the credibility of this transfer policy for capital and profit remains to be tested.

2. *Profit Remittances*

Article 22 of the new law continues to allow both repatriation of capital and profit remittances. In principle, foreign investors may transfer their share of profit and the transfer must be made in the year in which profit is earned. Foreign workers in FDI enterprises may also transmit their income overseas. Experiences with transfer of profit have been mixed: transfer of large amounts faced scrutiny while small amounts were often smuggled out in tens of thousands dollars by small firms. Both large and small investors complained about difficulties with getting clearance from tax offices prior to transfer of profit. The most celebrated case involved Peregrine, a Hong Kong-based investment group that was among the first major foreign investors coming to Vietnam and one of the few success stories turned sour. The group was charged with tax evasion and its Resident Representative has been barred from leaving the country until the case is settled. As the Vietnamese currency, the Dong, is not convertible and the law does not explicitly guarantee conversion, there may be a practical problem of foreign exchange availability for purpose of repatriation and remittances. The issue of profit remittances and repatriation of capital in the case of Vietnam, as in other developing countries, is thus as much an economic problem as a legal issue.

H. Rights to Hire and Fire

Labor relations in FDI enterprises are regulated by a separate decree[12] (Labor Regulations for Enterprises with Foreign Invested Capital). As reflected in this regulation, an FDI enterprise's right to hire is more constrained than the right to fire. Minimum wage is set currently at $50 (U.S.) per month (some firms pay more, such as Coca-Cola $80 (U.S.), and Reebok $67 (U.S.), which is still higher than wages paid by a local enterprise, although local wages are increasing with expansion of the industrial sector. FDI enterprises are required to give priority to Vietnamese nationals when recruiting employees. Expatriates can fill a position when no Vietnamese nationals with comparable skills are available. Hiring is further constrained by the fact that foreign investors must either select employees recommended by a local government labor agency, or by asking these agencies to do the recruitment. Direct recruitment is allowed only when these agencies fail to provide the required labor and notify the labor agency. As the country had almost no private labor contracts under its previous centrally planned economy, detailed formats as well as circumstances for termination of labor contracts were specified for the first time in the decree on labor regulations for FDI enterprises. According to this decree, as in market economies, workers may be fired in the following six instances: 1) consistent failure to carry out assignments; 2) dishonesty; 3) violation of the rules of the enterprises or labor (work) discipline; 4) illness, injury or disablement not curable or remediable within six months; 5) stoppage or reduction

12. Decree No. 233, HDBT, June 22, 1990.

of production in case of *force majeure*; 6) reduction of production as a result of reorganization due to changed technology or management.

In the past four years, sporadic labor disputes leading to brief strikes have been reported. Incidences of labor problems related to the worker/supervisor relationship, abuses and sexual harassment have occurred in several foreign firms. In 1996 a much publicized labor relations problem involved Nike Vietnam, which has a subcontracting arrangement with the Korean firm Sam Yang to run its Vietnam operation. It was accused of creating sweatshop conditions such as unsafe work environment, low wages, and long hours After this and other incidents, foreign firms felt the need for staff training programs focusing on cultural aspects of industrial activities in Vietnam.

Potential conflicts over labor problems between foreign investors and local partners also may arise when foreign investors, if eventually permitted, gain entry by way of privatization of SOEs. As most SOEs are over-staffed, foreign investors would like to see reorganization and streamlining, but will find both difficult to achieve given the deep-rooted egalitarian culture of SOEs in Socialist Vietnam that makes management unwilling to fire workers.

The Ministry of Labor oversees the enforcement of labor contracts and relations. Trade union laws, which recognize workers' rights to form trade unions normally associated intimately with the Communist Party, are also applicable to FDI enterprises. Labor disputes have to be first negotiated for settlement, and when this fails the two sides can choose between a reconciliation council chaired by an official of the Ministry of Labor and consisting of an equal number of representatives from the two sides, or an arbitration council established and chaired by an official of the Ministry of Labor. The current law does not provide remedies through court action.

I. The Physical Enclave: Export Processing Zones (EPZ)

Vietnam's enclave-based FDI strategy includes a physical enclave in the form of EPZs, which are fenced zones. EPZs are new in Vietnam, where the first two projects approved have completed construction (the first one is the Tan-Thuan EPZ and the second one is the Linh-Trung EPZ, both in the outskirts of Ho Chi Minh City), and most parts are in operation.[13]

Generally speaking, the EPZ Regulations provide investors inside the Zone more generous fiscal incentives than the incentive package for foreign investors operating outside the Zone under the general Foreign Investments Law. Efforts were also made to remove some of the constraints in the FDI Law, as applied to EPZ investors. For example, EPZ investors are not required to comply with the minimum wage as under the FDI Law although they are expected to give hiring priority to local labor.

According to the EPZ Regulations, an investor has a choice, within the fenced zones, between renting a slot to construct individual factories, or leasing or purchasing factories built by the government or the EPZ Construction Company. Approval of applications for establishing EPZs is by the authority of the Ministry of Planning and Investment (previously State Committee for Cooperation and Investment), which is also charged with overseeing implementation and administration. The procedure for approval of EPZ projects is similar

13. For operational details and economic issues of Vietnam's EPZs see VIETNAM: POLICIES FOR TRANSITION TO AN OPEN ECONOMY, UNDP/WORLD BANK TRADE EXPANSION PROGRAM COUNTRY REPORT, ch. 6 (1993).

to that for other foreign investments projects. The EPZ management, called EPZ Construction and Trading Company, screens admission of individual investors. The duration of EPZ enterprises is fixed at fifty years and can be extended.

As with the FDI special incentive package, the issue with EPZ is not so much its legal framework per se as Vietnam's use of other countries' experiences[14] to set out a standard policy/legal framework for its EPZs. As with FDI special tax treatment, the broad issue regarding EPZ is its enclave nature, which will not serve the country's long-term interests. Additionally, as shown in several studies, EPZs generally incur high costs and achieve a low rate of success and fewer direct benefits to the host country than expected.[15] For the time being, using EPZ as one of the instruments to provide free trade status to export activities for international competition can be suitable for Vietnam in the absence of a liberalized trade policy. EPZs in other words, are only a transitional policy/administrative instrument and should be part of, not a substitute for, a larger program of policy reform for export development. They should be phased out when trade is completely liberalized.

In general, legal enclaves for FDI and physical enclaves such as EPZs are both temporary development instruments that should be used with time-bound validity and phasing-out procedures in place.

V. Regulatory Impediments to Foreign Investments

A major problem with Vietnam's FDI is its slow pace of implementation, similar to China's FDI situation in the early years of its open door policy when the FDI implementation rate was in the range of thirty to forty percent.[16] Several factors were responsible for this slow pace of implementation; most of them are rooted at the country's bureaucratic system, which also created tremendous impediments even at the initial stage of the investment approval process. This section reviews some of the more pertinent problems with regulations affecting foreign investors' decision to invest and the pace of implementation once the project has been approved.

A. Problems in Approval Procedures

1. *Bureaucratic Process*

The basic law on FDI, the Foreign Investments Law reviewed previously, set out only the broad principles for FDI and established the State Committee for Cooperation and Investment (SCCI) headed by a cabinet minister in charge of FDI. In 1995, SCCI was merged into the Ministry of Planning that became the Ministry of Planning and Investment, in charge of planning and foreign investments. Subsequent regulatory laws, mainly in the form of decree, arrete, and circular for application created a myriad of paperwork constituting a complicated process for FDI approval. Like China, which also has a complicated FDI bureaucratic process, but unlike Eastern Europe, where there is either no process or a simplified process for FDI[17], Vietnam has a system of sanctioning or approving investment

14. The co-general manager of Tan Thuan EPZ financed by Taiwan capital was also the general manager of the well-known and successful Kao-Schung EPZ near Taipei.

15. For empirical research results, see Donald Keesing, et al., World Bank Country Economics Department, Export Processing Zones (1993).

16. *See* Lafar Shah Khan, Pattern of Direct Foreign investments in China, World Bank Discussion Paper No. 138 (1991).

involving too many approval agencies of both the central government[18] and provincial government level. As a result, this multiplicity of approvals takes much longer than the mandatory three months from the date of the application, as stipulated in the FDI Law. A recent study based on a sample survey of the private sector[19] indicated that the most serious impediment to foreign investments in Vietnam has been problems with the legal and regulatory framework affecting the process of project approval and project implementation.

A major problem in the process of approval is the overlapping authority of local government, mainly at the provincial level, with the central government. Currently, the central authority (Project Evaluation Committee) in Hanoi evaluates the proposed projects according to nine criteria. Some of these criteria (e.g., legal status of the company, project sponsor's financial situation) are already on the list of five criteria used by provincial governments that, as in China, at times seem jealous over their new found authority as a result of decentralization.

In accordance with a Ho Chi Minh City's provincial circular that established a new evaluation unit to exist in parallel with the local SCCI, now a branch of PMI, and the Central SCCI now part of MPI, a foreign investments project proposal in Ho Chi Minh City must pass through three layers: (i) eight copies of the project-proposal should be submitted to the City People's Committee and its Committee for Cooperation and Investment Evaluation (Project Evaluation Committee of the City) for evaluation; (ii) following a clearance from the City People's Committee, the local SCCI reviews the project to ensure it is in good order before passing it on to the Central SCCI in the capital city of Hanoi; and (iii) the Central SCCI will approve or reject the project upon recommendation of the Central Project Evaluation Committee chaired by the Minister of Planning and Investment.

Complicated approval processes for FDI and investment are not unique to transition economies, but are common to most developing countries regardless of political orientation. However, skepticism and lingering suspicions vis-a-vis capitalist investors also play a role in Vietnam's control-based FDI approval system. Even within this cautious attitude, improvements can still be made, along with other procedural streamlining, by collapsing the three-step process into a single one, eliminating bureaucratic layers involved in essentially the same assessment process, which duplicates paperwork.

The number of approval agencies at the Central Level can also be reduced considerably to less than the current eight. For example, the Central Bank (State Bank of Vietnam) should be involved at the implementation stage when financing is required. Similarly, the Ministry of Science may have a role later in the process when transfer of new technology may become an issue. The planning branch of the MPI should not be burdened with project review when the country has basically eliminated the concept and practice of central planning. The reduction of the number of approval agencies also strengthens the sanctioning authority of MPI and is an essential step towards the contemplated one-door service institution.

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17. *See* GRAY, *supra* note 7; *see also* KHAN, *supra* note 4.

18. At the central government, approvals are required from eight agencies including the State Planning Commission, Finance Ministry, Ministry of Commerce and Trade, Ministry of Science, Ministry of Construction, State Bank (Central Bank) and "other Ministries relevant to the sub-sector in question." Cabinet Decision No. 366, HDBT, Nov. 7, 1991.

19. FOREIGN TRADE & INVESTMENT DEVELOPMENT CENTER (FTDC), VIETNAM: A SMALL PRIVATE SECTOR SURVEY, FINANCIAL SECTOR REVIEW MISSION (1995). The survey was supervised by the author of this paper who participated in the mission.

The ideal way to remedy process problems resulting from procedural laws is to have no process, as currently is the case in many CEE countries, for no optimal process can exist in a large bureaucracy. The second-best solution is to streamline the process, cutting out as much as possible the institutional layers and their attendant regulatory requirements.

2. *The Feasibility Study Requirement*

A FDI is required to have a feasibility study. As long as the country has trade barriers, the government will be interested in the economic analysis (the core of a feasibility study) of the project to ensure that the project is not harmful economically—not proposed for negative value-added industries at world prices. However, most, if not all, of the feasibility studies submitted to SCCI are only simple pre-investment studies subject to further detailed engineering study prior to project implementation. But even if these studies are sufficiently detailed and properly done, including a cost/benefit analysis with the use of proper shadow pricing, these studies are most useful to financing institutions, which should gauge the financial viability of the project in making their lending decisions. Furthermore, moving the incentive structure close to world prices would reduce immensely the whole problem of economic analysis. In the meantime, when the incentive structure is still distorted as in Vietnam, feasibility studies and particularly economic analysis therein should be required for large projects and not for smaller scale projects.

B. Problems in Implementation

Once the long-awaited approval of the project proposal is obtained, foreign investors must confront a variety of problems in implementation. The problems arise from start-up to the time the project is on-stream. These problems include the country's notorious corruption, which is pervasive and known to the government but hard to document. A recent study reveals some of the more common problem areas reported by foreign investors.[20] Some of these problems are often found in other developing countries, while others, particularly the legal framework issues, are typical of an economy in transition. Several FDI projects have been withdrawn due to such obstacles. Apart from the early birds mentioned earlier, Mitsui of Japan, Petronas of Malaysia, the mining company Austing of Australia, City Horse of Hong Kong, and Australia's ACP, which used to participate in the well-known publication *Vietnam Investment Review*, are among the other frustrated investors who are leaving Vietnam. Implementation problems caused delays in production, resulting in increases in sunk cost (just as approval problems did), and affecting project viability. No study on the financial performance of FDI in Vietnam is available, but events and pronouncements by investors point to a negative assessment. For example, Procter & Gamble (P&G), the Cincinnati, Ohio-based toiletries giant, launched its Vietnam operation in 1996 with a $14.3 million joint venture. Reportedly, P & G has lost $28 million so far and had to consider increasing its investment to survive or face bankruptcy. The company said that costs have since proven "significantly higher" than expected.[21] James Rockwell's consulting business, Vatico Inc., whose clients included Chrysler, IBM, Hughes Aircraft, and Amway Corp, was the first American company licensed to operate, but closed its doors on June 30, 1997, after six years in Vietnam. In Rockwell's opinion, "If ten percent of foreign invested companies in Vietnam are making a profit, I'd be surprised."[22]

20. *See id.*
21. *P&G Seeks to Raise Investment in Vietnam to Avert Bankruptcy*, Bloomberg News, Oct. 20, 1997.

C. Start-Up Problems

Most of the start-up problems of implementation were caused by red tape at the local government level. Start-up problems include difficulties with clearing the site and delays in securing building permits, power lines, and water supply. Delay is also common in importing machinery and equipment as a result of difficulties in obtaining an import permit in custom clearance. To accomplish all these steps, investors must complete a myriad of paperwork for numerous large and small bureaucracies and, in many places, face corruption in the form of bribing (referred to as toll gates[23]) to expedite the process.

D. Problems at Operational Stage

When the project goes on stream, the foreign investor must confront more problems, many related to the regulatory framework. Two areas in which the investor would have to deal in the course of managing its daily businesses are the restrictive and highly protective trade regime[24] and the financial sector, in which banking activities are limited by restrictive regulations and borrowing is constrained by an unstable legal system that does not recognize private ownership of land preventing the use of real property as collateral for lending purposes. The problems in both areas are deep-rooted in Vietnam's control-based policy for both trade and banking, which created an ever-increasing number of rules and regulations. These regulations change through the implementation of a project.

1. *Trade Restriction*

a. Subsector Restrictions

Two major problems with Vietnam's trade laws have caused many difficulties for investors: the subsector restriction and the highly protective foreign trade regime that is effectively biased against the private sector, both domestic and foreign. The 1990 Law on Private Business (art. 5) lists seven sectors that require investment permission from the Prime Minister himself: (1) production and trading of explosives, poisons, toxic chemicals; (2) exploitation of all kinds of precious minerals; (3) production and supply of electricity and water on a large scale; (4) production of facilities for communication broadcast, services related to post and telecommunications, radio and TV broadcast, publishing; (5) sea and air transport; (6) import-export trading; and (7) international tourism. Many of these sectors, such as import/export, are routine activities of the private sector in a market economy and should be liberalized. This particular restriction on subsectors has in effect created a virtual monopoly in foreign trade for State enterprises; of the thousands of trade permits issued, only a handful are given to the private sector. Private trading firms must go through one of over a thousand SOEs who hold trade permits and act as intermediaries for a fee (officially, a commission of one percent is charged). This is perhaps the most serious reg-

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22. *First U.S. Investor to Vietnam Heads Home, Others May Follow*, Bloomberg News, May 29, 1998.

23. The term was used most recently in a speech. Jules Carson, Chair of the American Business Community in Ho Chi Minh City, Vietnam: Great or Not-so-Great for Foreign Investments?, Speech (June 1998). Carson said, ". . . There are simply too many toll gates, ministries, customs officials, tax collectors, inspectors, People's Committees, quotas, licenses, chops, etc. than many managers can manage and still run a profitable business . . ."

24. Vietnam: Policies for Transition to an Open Economy, UNDP/World Bank Trade Expansion Program Country Report chs. 5 & 6 (Sept. 1993).

ulatory impediment to private sector development as trade liberalization is a crucial step in the transition to a market economy.

b. Trade Policy Restrictions: High Tariffs and Quantitative Restrictions (QRs)

Vietnam's current trade policy and trade laws are highly protective, featuring both QRs and a widely dispersed tariff structure. Investors may benefit from protective tariffs and QRs in favor of their domestically produced goods, but a highly protective trade regime is biased against export activities and in the long run will not promote efficiency of domestic industries, including those developed by foreign investors. Vietnam's current tariff schedule contains as many as twenty-five rates varying from one to 200 percent C.I.F. values. Variations in tariffs are harmful—even more harmful than high but uniform tariffs—because they tend to shift resources to inefficient activities. As a result of this trade policy, several major foreign investments projects have been proposed for such inefficient but protected industries as car and scooter assembly. The need for Vietnam to liberalize foreign trade is a persistent subject of debate within the government and by aid donor countries. The government took some initial steps towards liberalization, but further progress will be slowed by resistance from vested interest groups including protected industries, the control mind-set of policymakers, and lack of understanding of the complex relationship between trade liberalization and growth. Under these constraints, Vietnam's international competitiveness beyond some traditional exports will be slow to improve.

2. *Banking Problems and Lack of Financing*

In principle, foreign investors are allowed to borrow from the domestic capital market. In practice, while working capital is available to a few customers in a limited number of export industries, term financing beyond one or two years is not available in the country's nascent banking system. Currently, both domestic and foreign investments are self-financed, although in a strict legal sense, firms can be leveraged up to seventy percent (only thirty percent to be paid-in, which is the amount of legal capital required). The lack of financing and undeveloped banking system forced foreign investors to arrange financing overseas, which resulted in slower implementation and high transaction costs. The country's almost non-check banking system and the system's newness impose further constraints on project implementation as all transactions are carried out in cash. A number of recent regulations restricted further banking activities, particularly foreign banks. For example, a November 1997 regulation by the State Bank (Central Bank) limited open positions on hard currency held by foreign banks to less than $2 million; any bank with more than that would be forced to sell on the interbank market. Such a requirement would reduce competition and increase the cost of raising investment capital. A November 1998 regulation requires further that banks must sell for local currency (Dong) eighty percent of all foreign currencies held by firms. In view of this rule and the unstable Vietnamese currency, it is likely that foreign firms must keep most of their foreign exchange holdings in off-shore accounts. A 1997 regulation on checking accounts illustrated Vietnam's tendency to over-regulate and restrict its newborn banking activities.[25] According to this regulation, Vietnam, unlike other countries in South East Asia where checks are valid for six months and can be written in English, has ruled that checks are valid for only fifteen days and must be written in Vietnamese

25. *See e.g.*, Asia Times, Mar. 13, 1997.

(English could be added but in smaller letters underneath). The first letter of the sum in words must be capitalized and there must be no blank spaces or mistakes in filling out the checks (e.g., initialed correction is not allowed.) Furthermore, checks must be one exact size specified by the State Bank, and must be printed by the State Bank's print shop, which has no capacity for security printing common in other countries. For companies, the chief accountant must countersign every check. In addition, individuals are only able to purchase one book of ten checks at a time, and companies are only allowed three ten-check books. The above regulations have discouraged the use of checks as means of payment in Vietnam, where in 1997 a population of 75 million people held fewer than 41,000 checking accounts. Because of these regulatory constraints, Vietnam will remain a cash-based society for a long time. But the most damaging regulation was a recent decision by Vietnam's Supreme Peoples Court, which ruled that banks are not responsible for the letters of credits they issue. This unusual decision speaks not only to the unreliability of Vietnam's banking system, but more seriously to the unpredictability of the country's legal system.

E. Regulations for Domestic Investment

Domestic investors have not been in a better position than foreign investors. All the studies done in recent years[26] on Vietnam's emerging private sector reveal the same obstacles to domestic investment but in a different order; they include among other things, a poor basic physical infrastructure, a primitive banking system and an unstable system of laws and regulations. Unlike foreign investors, domestic investors worry less about legal framework problems than other impediments, such as the lack of bank financing. Like other Asian investors, they are accustomed to dealing with in an informal legal framework.

In general, Vietnam's reborn private sector must operate within a more restrictive regulatory framework[27] than do foreign investors, in part because the government is still struggling with the philosophical issue of how compatible a liberated economy and an expanded private sector can be with a socialist political structure. Unlike their colleagues in Eastern Europe, Vietnam's policymakers do not have a clean slate upon which they may promote private investment and private sector development.

For the domestic investor, the process of investment approval is less clear, but not as complicated as the one for FDI; it also involves a time-consuming period of security investigation prior to registration and project evaluation. Beyond approval, domestic investors like foreign investors must face a host of regulations affecting implementation including import/export restrictions, land regulations, utilities problems, a deficient banking/credit system, and an uncertain legal framework.

Two new laws, the Company Law and Private Business Law, while helping to clarify the forms of doing business, do not help promote deregulation. The Law on Companies (Company Law) essentially reintroduced two French-style companies of limited liability familiar to Vietnam's private sector—the Societé Anonyme (SA), similar to a corporation and the Societé a Responsabilité Limitée (SARL), somewhat similar to a limited partnership. In addition to the Company Law, Vietnam has a Law on Private Business, enacted December 2, 1990, that is essentially a detailed limitation on what is already in the new Constitution

26. *See, e.g.*, *Per Ronnas: Employment Creation Through Private Entrepreneurship in Vietnam*, ILO/SIDA(1992); FTDC, *supra* note 19.

27. For a detailed analysis, see Van Thuyet, *supra* note 9.

regarding the extent to which the private sector can do business. This kind of law, basically redundant in a market economy, may be necessary for assurance of the legality of commercial activities by the emerging private sector. In a matured market economy such a law should not be on the books. In its efforts to reestablish a market economy, Vietnam should resist the temptation to go overboard in making new laws. A liberated economy requires fewer instead of more laws beyond the basic codes or statutes.

Apart from restrictions on seven subsectors requiring the Prime Minister's permission as mentioned, the Law on Private Business imposes further entry barriers through a minimum capital requirement for each activity of private businesses. This type of restriction is not found anywhere else in Asia. The law lists minimum capital requirements for eighteen activities, ranging from $25,000 for hydropower (probably activities supporting a hydropower plant), the highest, to $2,500 for handicrafts and restaurants, the lowest. A similar list for companies is also attached to the Company Law, with capital requirements roughly ten times higher than those for the corresponding unincorporated enterprises. The Law on Private Business contains a final clause to deal with violations of the law, mainly noncompliance with business license regulation and change of activities without permission. Curiously, the clause envisages criminal prosecution for these purely civil actions. However, no penalty is specified.

VI. Substantive Law Issues

As discussed in the previous section, procedural problems have presented major obstacles to foreign investors when they first consider entering Vietnam, and unresolved issues of substantive law discovered in the process of dealing with their local counterparts, the government and the laws have made investment decisions more difficult. This section reviews some of the more controversial issues causing concern to most foreign investors but remaining largely unresolved. Those issues are corporate governance in joint ventures, land use rights and intellectual property rights.

A. Issues in Corporate Governance for FDI

Regulations on corporate control and monitoring for FDI enterprises are in the Foreign Investment Law. Some provisions of the FDI law regarding organization are similar to the Company Law, but many others depart from it. Because Vietnam's Company Law is not applicable to FDI, comparisons between the two laws would show a bias against foreign investors. For example, the form of management organization specified for a FDI enterprise is broadly in line with the provision of the Company Law for domestic organizations which includes the Board of Management, the Director General, and other specified officials, but the voting rights of board members in a FDI firm do not reflect proportional shareholders' rights as in the Company Law. Other significant deviations from the Company Law and normal practice in other countries are demonstrated by the rules of decision-making and the prerogatives of the company officers of a FDI firm. In a joint venture, the parties appoint members to the board of management in proportion to their capital contribution. However, both parties must have at least two representatives each on the board of management, regardless of their capital contribution. Furthermore, if more than two parties are involved, the minimum number of board members is one seat per party involved, regardless of their respective proportional holdings.

B. Two-Captain Ship Clause

Unlike the Company Law, which refers the Board's decision-making rules to the by-laws for joint ventures, the Foreign Investments Law stipulates in Article 13 of the old FDI Law that decisions on "principal matters which relate to the organization and operation of the joint venture, namely its business objectives, business planning, and key personnel," may only be made by a unanimous vote of the board. This effectively gives each party involved the power to veto any decisions on these matters, a situation dubbed a two-captain ship clause by foreign investors in Vietnam. This veto provision is clearly a major impediment to effective management, goes against the rule of majority based on proportional holdings, and has deterred many foreign investors from forming joint ventures in Vietnam. All other decisions must be supported by a two-thirds majority. The chairman of the board must be appointed by consensus, but the law is silent about the chairman's powers. The new law still retains this principle of unanimity but spells out the areas of its applicability, including the appointment of the Director General (President), the First Deputy Director General (First Vice President), the Chief Accountant (Treasurer), the amendments of By-laws, approval of financial statements, and decisions on construction projects and borrowing for investments (art. 14). The new provision thus removed the uncertainty inherent in the old overbroad provision, but still constrains efficient management of a joint-venture enterprise and limits the authority of foreign partners who almost always represent the majority of shareholders as they normally contribute seventy percent of the joint-venture's capital.

C. Land-Use Rights Issues

As Vietnam still maintains its communist regime, all land belongs to the State in line with socialist ideology, (or "belongs to the People," according to the language of the Constitution). To circumvent this legal obstacle to transition to a market economy, in which ownership of real property normally remains private, Vietnam, like China, developed a legal framework for real property based on long-term land-use rights in order to establish a market for real property. Land-use rights in this form constitute quasi-ownership. This quasi-ownership includes rights to use, to usufruct, but not to sell real property.[28]

Land-use rights may be transferred, although the land itself cannot be transferred. Land-use rights were defined for the first time in the Land Law, then later in Part V of the Civil Code promulgated on November 9, 1995. The Code discusses in four chapters various forms of ownership for personal and real property. For the latter, the Code reiterates the concept of state ownership of all land. For business purposes, the Land Law that contains details translating the concept of state ownership of land into practical application is more relevant than the Civil Code.

As in other areas of laws, land law evolved in response to reality and changing political orientation. Prior to 1988, there was no need for a land law, as private farming was not allowed in rural areas, and private business was almost non-existent in urban areas. Land

28. Article 14 clarifies what specific decisions require unanimity of vote: "The most important matters of organization and activities requiring unanimous vote of members attending Board meeting for decisions are: appointment of Director General (President), First Deputy Director General (First Vice President), Chief Accountant (Treasurer), amending Bylaws, approval of Annual financial statements and construction projects, and borrowing money for investment."

management was conducted through administrative decisions at local government levels. The new Land Law promulgated on July 24, 1993, and its attendant application decree provide details on the hierarchy of types of property ownership and set out the regulations on the right to use, to inherit and to transfer the right to use.[29] In practice, the land-use right system encountered numerous problems both because of ambiguities in the legal texts and frequent changes of black letter laws.

For foreign investments, land-use rights have created two major problems: one relates to evaluating the value of land-use rights in the real property market and the other relates to the recent transition of land-use rights into rents.

1. *The Pricing Problem of Land-Use Rights*

The Land Law categorizes six types of land for the purposes of charging fees for use, and for property tax, rentals and compensation in case of retrieval (re-expropriation). The six categories are 1) agricultural land, 2) forest land, 3) rural settlements, 4) urban land, 5) land for specialized uses, and 6) unutilized (green field) land. There is a basic rent schedule for each region, which may change over time. Until recently, most homeowners in urban areas paid property tax on land but not fees for the right to use it. For foreign investments, contribution by local counterparts to most joint ventures was almost always in land-use rights for which the value is uncertain and has become the subject of protected negotiations. Partly for this reason, foreign investors sometimes prefer the 100 percent foreign-owned form of investment.

2. *The Instability of Land-Use Rights Laws: Land-Use Rights vs. Rents*

Two new laws, in the form of decree/circular, have changed the land-use rights situation in Vietnam and caused further complications for foreign investments. The first law[30] requires the collection of 100 percent of the new fee assessed for land-use rights to be paid by the holder or seller. The new fees charged for land-use rights are very high. In some areas in Ho Chi Minh City (Saigon), the fee may be as high as $1,300 per square meter. The new decision has also frozen the real property market because the new regulation on land-use rights increased real estate prices enormously. This decision has caused strong protests from homeowners. Ho Chi Minh City has petitioned the central government to review and rescind the circular.

The second law,[31] which requires all land-use rights on commercial properties to be transformed into land leases, has caused an even stronger protest and created considerable confusion. With regard to foreign investments, the new regulation raised a new issue of land value contributed as equity by the Vietnamese counterparts in joint ventures with foreign investors. As mentioned, for joint ventures in Vietnam, the contribution in equity by the Vietnamese side has almost always been in the form of land-use rights acquired by state-owned enterprises—these enterprises in effect own land on behalf of the state by virtue of their state enterprise status. When the land is to be used as equity in a joint venture with foreign investors, the dollar value of this land or the land-use rights has been the subject of intense negotiations between foreign investors and their local counterparts. The local

29. For a detailed treatment of Land Law and other property laws, see Van Thuyet, *supra* note 9, at 548–56.

30. Finance Ministry Circular No. 02.

31. Decree No. 18, Feb. 13,1995, applicable retroactively to Jan. 1,1995.

counterparts typically would claim they wanted to contribute fifty to fifty-one percent of the assets of the joint venture, regardless of the size or location of the lot. The final settlement is usually the result of a bargain with no rational basis to support it, but the land value is never fixed at less than thirty percent of the assets of the joint venture to be formed. Under the new law, the value of land is reduced to the rentals the Vietnamese counterparts must pay the government since they now no longer own land-use rights but simply a right to sublease or assignment; the value of their long-term land-use rights normally is greater than the rents they must pay the government. Foreign investors now claim a downward revision of the equity contribution by local counterparts, but in practice they have not succeeded, as the whole issue of implementing the new law remains unresolved.

The new regulation in effect nullified the quasi-ownership of land intended under the concept of long-term land-use rights. The regulation has made the land law more unstable and is a fearful example of the unpredictability of Vietnam's legal framework to the extent that an administrative decree can change substantive law.

Apart from creating confusion for FDI management, the new regulation seriously impacts the working of the financial market. In principle, mortgaging of real property is legally possible based on provisions of the Land Law (art. 3) which allow pledging the land-use right, and of the Housing Law (art. 7), which allows pledging of the house attached to the land. In practice, mortgages were rare because of difficulties in ascertaining title and problems involved in foreclosures. Some domestic banks in Ho Chi Minh City began to accept, on an experimental basis, ownership papers for residential houses and commercial buildings as collateral for short-term loans. The new regulation is causing disturbances in the financial sector because banks no longer accept land-use rights as collateral for loans. In fact, some banks have started to recall loans made previously on the basis of land-use rights.

D. Protection of Intellectual Property

Protection of intellectual property has been a major concern of foreign investors particularly when their businesses are based on proprietary technology, such as brand name products in garment and footwear industry (Nike, Adidas and Reebok), in soft drinks (Coca-cola and Pepsi Cola) and in pharmaceuticals. On June 27, 1997, Vietnam signed an agreement with the United States on copyright protection. It remains to be seen how the agreement will be implemented.

Vietnam's legal reform roughly parallels China's efforts[32] both in areas covered and in terms of timing. Various ordinances and decrees[33] protect four other intellectual properties in addition to trademarks, which is the most important intellectual property in the context of Vietnam's transition: patents, utility solutions, industrial designs, and appellation of origin of products.[34] Another category called industrial secret (trade secret) was added[35] to

32. Decree No. 18, Feb. 13, 1995 and applicable retroactively to Jan. 1, 1995. *See, e.g.*, Ralph H. Folson, et al., Law and Politics in the People's Republic of China 372 (1992).

33. All five categories are governed by Decree No. 84 on Protection of Intellectual Property, HDBT, Mar. 20, 1990, Decree No. 201, HDBT, Dec. 28, 1988, and Arrete 49, HDBT, Apr. 3, 1991, on Transfer of Technology amending Decree No. 197, HDBT, Dec. 14, 1982. These texts establish both substantive and procedural laws for intellectual property protection.

34. Trademark is defined as a symbol used to distinguish goods or services of the same kind from different production or commercial units. Inventions are technical solutions that present "world-wide novelty" and represent an inventive step applicable in a socio-economic field. Utility solutions are defined as the application of an old (patentable) technology in a new and previously unused way in Vietnam. A registrant can obtain a

regulate the transfer of technology through licensing, although this category was not defined. Current laws provide the rights to possession, to use and to transfer over the protected objects. Most of the above laws on intellectual property have now been codified in Part Six of the 1995 Civil Code.

1. *Characteristics*

Vietnam's system of intellectual property protection adopts the "first to file" rule for the most part while most other countries adopt the "first to use" rule. About 50,000 trademarks have been registered under current laws. The use of the "first to file" rule could create litigation over an intellectual property that was pirated but properly filed prior to the authentic filing by the actual foreign owner. To remedy this problem, those who have utilized the property prior to and independently of the applicant for protection have the right to continue to use the property but are not allowed to extend the period of utilization or transfer it; and the government created a grace period for foreign owners to file their trademark on the basis of evidence that they were the "first to use," accommodating the legal practice of their home country. These measures will not settle the problem once and for all.

Some language of the law, while reflecting socialist features apparently cosmetic in nature, can be construed to create substantial regulatory impediments. For example, an owner of an intellectual right "is obliged to use or transfer in Vietnam in a way compatible with the need of social and economic development of the country."[36] This legal language provides broad discretion for implementation agencies to infringe upon ownership rights.

Another potential problem lies in the appropriation provision. Intellectual property can be expropriated if the Chairman of the State Committee for Science (SCS),[37] who is charged with overseeing the implementation of government policy in this field, "considers it necessary to use the protected invention, utility solution or industrial design for Vietnam's national defense or security or the prevention of treatment of human diseases or for other vital interests." Despite a provision for adequate compensation, the possibility of expropriation casts a shadow of uncertainty on Vietnam's intellectual property policy.

E. Enforcement for Protection of Intellectual Property

The duration of protection is generally fifteen years from filing date (China also provides fifteen years protection). The country is also a signatory of the Paris Convention, the Madrid Agreement, and the Stockholm Convention.[38] Vietnam's participation in these inter-

certificate that protects the new application for six years. Industrial designs are defined as the specific appearance of a product embodied by lines, three-dimensional forms, colors or a combination of these, which is new on a world-wide basis and capable of serving as a pattern for a product of industry or handicraft. Appellation of origin is the geographical name of a country or locality that serves to designate the origin of a product manufactured in that county or locality, provided that its qualities and characteristics are due exclusively or essentially to the geographical environment, including natural or human factors, or a combination thereof.

35. Decree No. 201, No. HDBT, Dec. 28, 1988.

36. Obligations of Intellectual Property Owners—Decree-Law No. 13, LOT/HDNN8, art. 13, Nov. 2, 1989

37. Now the Minister for Science and Environment.

38. The Paris Convention for the Protection of Industrial Property, Mar. 20, 1883, allows the owner of a trademark to claim a priority in a foreign country to the date of the initial filing in its home country. At present, there are more than 80 signatories to the Paris Convention. The Madrid Agreement, Apr. 14, 1891, allows

national protection conventions would greatly facilitate the flow of FDI and transfer of technology in the R&D-intensive sub-sectors and proprietary technology-based industries such as pharmaceutical and other chemicals where a good legal framework to protect proprietary technology is critical. In order to activate any of these agreements or any bilateral agreements for the purpose of securing protection or negotiation over technology transfer, the foreign party must state in the application letter its adherence to these specific agreements. Because of the newness of the field in relation to the country's transition to a market economy, Vietnam's legal documentation on intellectual property protection is at times confusing and should be strengthened.[39] Currently, a foreign owner of intellectual property must refer to numerous laws and regulations, including both the Decree-Law on Intellectual Property Rights and the Law on Technology Transfer, and several application arretes for an adequate coverage of the subject. The Law on Technology Transfer overlaps with the Law on Acquisition of Technology Through Licensing. Regarding transfer of technology, the issue is not so much legal as economic, involving not only the preparation of clear rules and regulations but also conceptual aspects of technology policy to be adopted.[40]

Protection against trademark infringement may be sought through the NOI, which can grant injunctions against the infringer and prevent future may infringements, but has no power to grant compensation for loss. In principle, remedies may be sought through the Peoples Court System. As Vietnam just reintroduced its market-oriented legal system, its courts have limited experience in dealing with these and other commercial matters.

VII. Legal Infrastructure and Law Enforcement

Despite legislative efforts in recent years, Vietnam's legal framework remains essentially informal and unstructured. There are laws on the books, but enforcement is weak. Regulatory laws in the form of decree, arrete, circular, and administrative decisions often overtake the basic statutes as has been the case of FDI legal framework. Law enforcement is not uniform but varies depending on the area of law and the parties involved in the lawsuit. Dispute resolution is conducted in People's Courts where lay assessors have the same powers as the judge. A concept of constitutional fairness and justice, akin to the notion of due process, has only begun to take root. This section reviews some of the law enforcement issues more pertinent to business activities, particularly foreign investments, focusing on commercial disputes.

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signatory parties who have registered a trademark in their home countries to register the trademark in all member countries by depositing a certificate of registration with the central registration bureau in Berne, Switzerland. The Stockholm Convention, July 14, 1967, established the World Intellectual Property Organization (WIPO), a U.N. organization that offers registration services for intellectual property and which facilitates the transfer of intellectual property from developed countries to the developing world.

39. For a Survey of Literature, see STRENGTHENING PROTECTION OF INTELLECTUAL PROPERTY IN DEVELOPING COUNTRIES: A SURVEY OF THE LITERATURE, WORLD BANK DISCUSSION PAPER No. 112 (Wolfgang E. Siebeck, ed. 1990). The study has a very extensive bibliography.

40. Several issues of this nature are discussed in RESEARCH POLICY INSTITUTE, UNIVERSITY OF LUND, SWEDEN, & INSTITUTE FOR SCIENCE MANAGEMENT, HANOI, VIETNAM, TECHNOLOGY TRANSFER TO VIETNAM: AN INTERIM REPORT, DISCUSSION PAPER No. 181 (1987); NGUYEN THAN HA, TECHNOLOGY TRANSFER TO VIETNAM, HISTORICAL AND CONCEPTUAL ASPECTS, RESEARCH POLICY INSTITUTE, UNIVERSITY OF LUND, SWEDEN (1989).

A. Vietnam's Legal Profession and Legal Education

Vietnam's legal profession is only emerging. Bar associations are being established, and offices of Notary Public in the civil code tradition, which requires a notary to have a substantial legal training, have been established in most cities. Professional judges and attorneys, particularly the younger ones, are trying to improve their legal education through continuing education and other programs. Lawyers' standing in society is also enhanced along with their earnings, which are no longer constrained by fee limitations. Apart from the more restricted bar association, each large city also has a lawyer association made up of professional attorneys as well as jurist, who are former members of the Judiciary or simply persons who are interested in the laws and have learned them on their own. Ho Chi Minh City and Hanoi, the capital, each have a bar association with membership requirements of training at a law school and passing a bar examination that includes, not surprisingly, socialist political doctrines. Ho Chi Minh City's Bar, with about 150 members, has been expanded in recent years to include several lawyers who had received their legal training in one of the law schools before 1975. This group of new attorneys has been trained in the standard law curriculum somewhat similar to the France's four- year law school program. Until recent years, these lawyers had not been allowed to practice because they were considered not politically able to function as socialist attorneys. After several years of reform and transition to a market economy, the government felt the need to have a corps of lawyers familiar with the market economy to help the judiciary cope with new types of litigation. Most of these capitalist lawyers were required to take short courses on Marxist political doctrines before being allowed to practice. The rest of the bar members received their legal training in the socialist tradition in Vietnam or in some other communist countries, and are unfamiliar with market-based legal systems, particularly in matters of contract and commercial law.

Several foreign law, firms including big names from the United States, such as Baker & McKenzie and White & Case have set up offices in Vietnam in anticipation of Vietnam 's booming private sector activities, particularly foreign investments. Foreign law firms, however, have discovered that their initial optimism is fading, first because foreign investments slowed down and also because their professional activities have been gradually restricted over the years. For example, beginning in 1995 foreign lawyers were not allowed to practice Vietnamese law. To overcome this limitation, foreign law firms hired local lawyers to file briefs prepared by foreign lawyers whenever local laws were involved; this practice has resulted in increased transaction costs and delay in the legal process.

B. Legal Education

Vietnam has begun to change its law school curricula to educate lawyers in a manner more suitable to market economy activities and to meet the needs of a society desiring more rules of law. The changed curriculum although sketchy, now reads much like a standard law school program in the West, except for a few traditional subjects on Marxism, a must in any Vietnamese school.

As in other areas of Humanities or Social Sciences, the problem with changing study programs to meet the needs of Vietnam's transition is the lack of educators to implement the new programs. The shortage is most acute in law and economics. The United Nations Development Program, The World Bank, the American Bar Association, and other groups in Europe have considered assistance in this area, but for a variety of reasons, including the government's reluctance to seek foreign assistance with its legal framework, not much progress has been made. Within the country, a group of lawyers trained in the West were allowed to set up a private law school in Ho Chi Minh City in 1994. In an attempt to control legal teaching, the school was ordered to close after one rather successful year in business, and folded into the state law school, which operates under government control. This was an unfortunate decision, as Vietnam needs more quality legal training institutions if it seriously considers introducing a rule of law system.

The quality of professional judges is crucial, as Vietnam's system of dispute resolution is inquisitional, in keeping with the civil code tradition, as opposed to the common law adversary system. This is an area of concern as legal training in Vietnam is in transition and the professional quality of judges is uneven.

C. Due Process in the Context of Socialist Vietnam

Vietnam has established procedures for both civil and criminal cases.[41] With the exception of the role of the Procuracy, Vietnam's civil and criminal procedures draw from the French codes. Vietnam's constitution does not use the term due process of law, but guarantees its citizens' property against nationalization, provides for compensation in case of nationalization, and requires that all arrests and imprisonment are done according to the rule of law. These and other provisions in the criminal law and procedure also seem to suggest the equivalent of due process of law. But there are constraints on how and what may be invoked to dispute a procedural or substantive law. To begin with, Vietnam has no judicial review of laws. The legislature reviews its own legislation and the laws of other government branches. Even if the validity of a law can be challenged, the question of whether or not a law or government act is deemed to be in furtherance of a legitimate governmental objective—to justify a deviation from substantive due process—should be understood in the context of Vietnam's centralized democracy (art. 6 of the Constitution) in which the Communist Party is "leading the State and the Society" (art. 4). In this context, it would not be surprising if the concept of compelling government interest, as often invoked in American law under the notion of substantive due process, would be broadened by the Vietnamese government under its system of centralized democracy. Similarly, a law that may restrict fundamental rights, such as freedom of speech and freedom of association, in violation of substantive due process in other societies, may not be inconsistent with Vietnam's concept of centralized democracy. For the same reasons, the notion of procedural fairness or procedural due process may also be subject to government's interests considered compelling or legitimate by Vietnam's government and its political system. In other words, due process of law in the Vietnamese legal framework must be related to factual context and ideology for its rationale and understanding.

As in other countries, due process of law in Vietnam or the equivalent of it is not a fixed notion. Its content changes with time and circumstances. For the time being, Vietnam's procedural fairness seems better observed in ordinary criminal cases than in cases involving political acts of opposition, which are often labeled as criminal or violating national security. Due process is also better practiced in major cities than at the district and local levels.

A setback for Vietnam's due process laws was the Prime Minister's decree No. 31 on Administrative Restriction on Persons, promulgated on April 14, 1997. The new decree

41. Decree-law for Civil Cases, Nov. 29, 1989; Code Crim. P., Jan. 1, 1989.

allows police and local governments to arrest and restrict movement of any person who is deemed to "have an act that violates the laws or harmful to national security as stipulated in Chapter 1 of the Criminal Code, but the act has not reached the level serious enough to be criminally prosecuted" (art. 2). The decree stipulated that "such person's movement will be restricted within his/her residence district, he or she may be relocated within the province if national security so required, will be forced to follow an reeducation program including reeducation through labor and to report Police once a month." The duration for such a measure will be fixed case by case as the decree does not fix the maximum period of restraint. In a different political system, such a of measure might have been an illegal or gross violation of both procedural and substantive due process, but presumably it was considered within the compelling interests of Vietnam's socialist government and therefore acceptable to it and to the judiciary.

D. The Court System and Adjudication Method

Vietnam's courts are divided into three levels, namely, courts of original jurisdiction, intermediate courts of appeal at the provincial level, and the Supreme Court. A central feature of this People's Court system is the collegial adjudication panel of three members, including two people assessors or lay assessors who, in principle, have the same powers as the judge. Economic matters specified but not defined in the laws establishing the court system, are being handled by economic courts that have two professional judges and one lay assessor for each sitting. In the trial court, judges as well as lay assessors decide both questions of law and fact. This is a cause of concern for litigants in disputes involving complex issues of law, such as commercial disputes. Rules of evidence are not applicable to all types of litigation, but are treated differently in each area of substantive law.

Vietnam's procedures have several features that distinguish them from both the Western civil code system and the Anglo-American system, including: (1) the role of procurator in a civil suit; (2) the ability of higher courts to choose at will to adjudicate any lawsuit being processed by a lower court; and (3) a procedure for retrial by committee of judges, called directorate adjudication (giam-doc tham), which is somewhat akin to administrative review.

In terms of subject matter jurisdiction, the trial court is the district court where most of civil law suits, including labor disputes, civil contract disputes (except economic contracts), and tort disputes are adjudicated except when the suit involves a foreign litigant, in which case the provincial court has jurisdiction. Grounds for appeal of trial court rulings are usually issues of procedure, and rarely issues of jurisdiction or substantive law. The Supreme Court may pick up without an intermediate procedure a lawsuit filed for adjudication in a lower court; in this case, the Supreme Court's decision is final.[42]

Apart from the regular appeal procedure, both civil procedure and criminal procedure allow for retrial through directorate adjudication. The retrial is conducted by a panel or committee of judges (directorate). The grounds for triggering this procedure are basically the same as for appeals, namely inadequate inquisition[43] (equivalent to discovery under common law, but by the Procuracy). Action for retrial can be filed within three years following the final judgment. To the extent a final judgment may not be conclusive, as should

42. Civ. P. Decree-law art. 11.
43. *See id.* at art. 71; Code Crim. P. art. 242.

normally occur under the principle of res judicata, litigants, particularly investors in commercial disputes, will feel legally insecure as a result of this retrial procedure. This particular procedure bears similarities to administrative review in the American and some other Western legal systems. It is not found in other socialist legal systems. The rationale for the procedure is probably the government's desire to add another layer of appeal in order to compensate for any deficiencies in the court system.

E. Independence of the Judiciary

The independence of judges, the courts, and of the Judiciary Branch in general is a relative matter in the context of socialist Vietnam where the judiciary is not regarded as equal to other branches of government. The Constitution does not state the principle of separation of powers; it requires the People's Courts to safeguard not only the socialist legal system but also the socialist regime itself (art. 126). The President of the Supreme Court, as head of the Judiciary Branch, is responsible to the National Assembly. Similarly, the chief judges of lower courts at provincial and district levels are to report to their corresponding local People's Councils. The Prime Minister appoints without consent of National Assembly all judges below the rank of the President of the Supreme Court. This process and the fact that the judges are not appointed for life discourages independence. In real life, private businesses and ordinary citizens have lost faith in the court system.

F. Vietnam's Procuracy

Vietnam's Procuracy is typical of a socialist legal institution that has no counterpart in any Western legal system. Comparatively, the Procuracy has power far beyond that of a U.S. district attorney or French public prosecutor.

According to Article 137 of the Constitution, the People's Procuracy has the power to supervise the legality of all government acts "to ensure that all government's acts and actions are legal, to serve as public prosecutor and to ensure that laws are implemented seriously and uniformly." Unlike the common law, the Procuracy may be active in a civil law suit. According to Article 28 of the civil procedure decree-law, the procurator may intervene at any stage of a civil suit on grounds of safeguarding the socialist (state) properties, of looking after the interests of workers in labor disputes, and of preventing certain unlawful domestic relations, such as unlawful marriage. In these areas, the procurator can initiate a lawsuit if no other interested parties seek action. For an investor, the fact that the procurator can get involved in a civil suit could complicate the litigation process by adding the government a an additional party, through the procurator. From a different perspective, a Procuracy can play a useful role in commercial litigation and can contribute to the functioning of the emerging market economy. But in reality, the Procuracy is more active in prosecuting criminal cases for which it is better equipped.

The Procurator General, Chairman of the Procuracy, is appointed by and responsible to the National Assembly. As such, the Procuracy is, in theory, a government branch of the same standing as the Supreme Court. In practice, the Procurator General is not only the most powerful jurist in the legal system, but also politically influential in view of his role as guarantor of socialist rule of law. Because of its broad powers, an activist Procuracy could threaten party and government control. On the other hand, the Procuracy is also required by the Constitution to safeguard the socialist regime, which makes its role quite delicate in critical times.

In sum, Vietnam's current court system is not independent. It continues to be constrained by ideology. Because the legal system continues to be unstructured and informal and law enforcement is weak, domestic investors and the private sector in general often avoid bringing their disputes to courts but prefer to settle them among themselves or with the help of the district People's Committee, which is regarded as more effective than the court.

G. Contract Enforcement and Dispute Resolution

Joint venture disputes often involve contract enforcement; parties in contract litigation are mostly foreign investors and their local counterparts, which are generally state-owned enterprises. Anecdotal evidence of breach of contract is an everyday concern among foreign investors. Foreign investors and their counsel would do well to familiarize themselves with Vietnam's contract law and resolution of contract disputes as Vietnam's legal system regarding these matters is complicated and frequently revised.

Foreign investors may choose to bring an action against their local partners in a local court instead of through the International Arbitration Commission (IAC). But the IAC is a better route because of its comparative competence and efficiency. Local counterparts may bring an action against their foreign partners in a local court, absent other stipulations in the joint venture agreement.

Vietnam's contract laws cover civil contracts and economic contracts, which are defined as "a written agreement between parties with the objectives of production, exchange of goods and service, study/research, application of scientific inventions and techniques, and other profit-oriented agreements."[44] Economic contracts reflect a Marxian concept of economic relationships and have long been a legal instrument in socialist Vietnam. Prior to the 1989 reform, economic contracts were designed mainly for to achieve a division of labor between state and cooperative entities. Subsequent decrees promulgated during the reform—Ordinance on Economic Contracts, September 25, 1989, and Implementation Decree, January 16, 1990—expanded the use of economic contracts to the private sector, including foreign investments in the context of a multi-sectoral economy, an economy that includes state sector, private sector and foreign investments. Economic contract was the only type of contract recognized and protected by the law before the general law on civil contract was introduced as part of the 1996 Civil Code.[45]

Vietnam's contract laws are restrictive in terms of capacity to contract. For example, only legal entities or persons with a registered business can enter in an economic contract (exceptions are made for some people having no business registration such as scientists, artists and fishermen). Provisions for enforcement and performance are unclear amd dispute resolution methods are uncertain. According to the pre-code laws, contracts must be in writing, i.e., oral or implicit contracts usually found in other countries' contract laws are not recognized or enforceable. The Civil Code itself, which codified most of the previous texts on civil contract, is silent on this aspect leaving the issue presumably for case law to settle. Exceptions are made for those without business registration, such as scientists, artists and fishermen.

44. Decree Law on Economic Contracts art. 1 (Sept. 25,1989).

45. Part III of the Civil Code deals with civil obligations and civil contracts while economic contracts are still governed by the above-mentioned ordinance.

H. Vietnam's Arbitration System

Prior to the establishment of economic courts in 1994, enforcement and resolution of disputes over economic contracts were handled by a system of arbitration that includes district and provincial arbitration offices and a higher level State Arbitration Office headed by a Chief Arbitrator that serves as the highest court of appeal for contract disputes. The State Arbitrator also hears cases involving an amount five hundred million Dong (approximately $50,000 (U.S.)) or more and all cases involving foreign parties, regardless of the amount in controversy. As with economic contracts, Vietnam has a tradition of dispute resolution by arbitration. The first arbitration body was established in 1955 to enforce contracts and resolve contracts disputes between state and cooperative organizations. The arbitrators are appointed by the Executive Branch of the government and work under the People's Committees (City or District Governments) or Central Government (for state arbitrators) although their decisions are binding like Court rulings. This type of dispute resolution authority, which is not independent, might have worked adequately in lieu of a proper court system in a centrally planned economy, but may not be sufficient in a mixed economy where contract disputes can arise between more diversified parties, including the state, the private sector and foreign investors.

The laws that establish jurisdiction of arbitrators over contract disputes do not exclude the People's Court System from adjudicating contract matters, but both the courts and the arbitrators have little experience in settlement of commercial disputes. Since July 1994, economic cases have been gradually transferred to the Economic Courts, which replaced the arbitrators. The new courts are staffed in part by the former arbitrators. These courts are intended to function like a circuit court specializing in commercial disputes. But the courts are in a formative stage, and their competence and efficiency remain to be seen. For this reason and many others, domestic investors often brought their contractual disputes to be resolved at the District People's Committee—part of the city government—instead of going to court or an arbitrator.

I. Arbitration on Cases Involving Foreign Investments

Foreign investors, particularly those from the West, find Vietnam's adjudication system unreliable because they are used to a stable, formal legal environment. The government is aware of this and has created an International Arbitration Commission to handle contractual disputes involving foreign investors, but it is too soon to tell whether it will be more effective than the existing court system.

The Commission is headed by a well respected, French-trained lawyer who was a member of the old Saigon Bar before 1975. In the majority of the decisions rendered since its inception, the Commission has ruled in favor of foreign investors. Unless specified in the disputed contract, the Commission has used the rules proposed by the International Chamber of Commerce (ICC) and the Convention on the Settlement of Investment Disputes between States and Nationals of Other States, along with other specialized rules relevant to the subsectors involved.

VIII. Conclusion

A. Toward a Better System: Open Policy Versus Enclave Strategy—A Good Start in the Late 1980s

Vietnam's Foreign Investments Law introduced in 1989, and amended in 1992 and 1996, was the first law introduced to open up the economy and initiate the transition to a market economy. As a result, a significant amount of FDI has occurred in Vietnam. However, implementation of FDI projects has been slow as about only thirty percent of the investments approved have been implemented. FDI projects have been concentrated in oil and gas, and hotel construction instead of diversified manufacturing. As a result, the effects on employment generation and transfer of technology from these sectors are not as beneficial as those that result from manufacturing.

B. The Decline in the Late 1990s

Since 1997, FDI in Vietnam declined substantially, which contributed to the decelerated overall growth of the economy. For years, foreign investors felt insecure doing business in communist Vietnam, and problems with the legal framework exacerbated by widespread corruption have been perceived as the number one impediment to investment. Several of the early comers have pulled out of Vietnam, tired of waiting for real reform to be introduced, including much-needed legal reform.

C. The Enclave Strategy

Vietnam's current legal framework for direct foreign investments is of the enclave type, in that a special regime is applied to foreign investments. A physical enclave in the form of Export Processing Zone (EPZ) has been in place since 1993. However, economic experiences have demonstrated that long-term development depends on both increased domestic and foreign investments. Ideally, there should be one regime for both FDI and domestic investors, with no enclaves. Experiences in other countries have indicated that incentive packages are not as important to foreign investors as a good investment climate.

A good investment climate would emerge with an open policy environment that does not constrain private sector development in general. Such a policy environment is normally created by a stable legal framework, a transparent and decontrolled regulatory framework, relatively liberal labor regulation, easy access to utilities, a good physical trade infrastructure, and a reasonably favorable living environment. In the case of Vietnam, while living environment is improved, other factors, particularly the policies and legal framework affecting private sector development based on both FDI and domestic investment, remain to be perfected.

D. Specific Problems

Vietnam's legal framework for foreign investments presents a variety of problems. Despite recent changes, Vietnam's approval process for FDI is still unnecessarily complicated; its regulatory framework also created serious impediments to project implementation by foreign investors. Following passage of the basic FDI law, a number of new laws were introduced to facilitate the transformation. Efforts to improve other areas of the legal infrastructure, however, are not comparable to law-making. This has resulted in an emerging legal framework featuring a superstructure made of newly enacted laws not adequately supported by a solid legal infrastructure. The legal framework has become unpredictable and unstable. More intensified efforts should be made to improve law enforcement. It would be a mistake to introduce new laws without parallel efforts to effectively implement them, for laws only work if they are enforced.

Several problems with substantive law, including the thorny issues of corporate governance in joint ventures and land-use rights, remained unresolved. Apart from the systemic problems caused by the lack of an independent Judiciary and deficient due process, Vietnam's court system and adjudication methods will be improved only with better training for lawyers, including judges and other court personnel, members of the bar and above all, the teaching staff of law schools, where new curricula and teaching methods have yet to be established. Extensive training of existing legal professionals is key.

E. Prospects

It is unclear whether the Vietnam's government would be willing to undertake further reform. But it would be unfortunate if Vietnam's leaders leave unfinished the transition to a market economy. Despite recent setbacks, Vietnam still has great potential for development and prosperity. It has proven to be a country of high growth for a decade and seemed to be on the way to becoming a new "tiger" in Asia. While the last two years have seen an economic downturn and recent performance of foreign investments is disappointing, Vietnam can still recover and return to a high growth path. Whether Vietnam may return to the "Trail of the Tiger,"[46] or remain only a "wild cat"[47] would depend to a large extent upon whether the government and the communist party leadership are willing to undertake real reform, particularly the legal reforms that remain incomplete.

46. *See* James Riedel, In the Trail of the Tigers, published as an appendix to the World Bank/UNDP joint report VIETNAM: POLICIES FOR TRANSITION TO AN OPEN ECONOMY. The paper reflected an optimistic view of Vietnam in the late 1980s.

47. *See* Pham Van Thuyet, Vietnam: A Tiger or Wild Cat (Nov. 1997) (unpublished paper presented at Columbia University). The paper discusses Vietnam's economic downturn for the past two years and prospects for the future.